# State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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Notice of Adoption and Filing of Examination Report

Take notice that the proposed report of the market conduct examination of the

1ST AUTO & CASUALTY INSURANCE COMPANY
2810 CITY VIEW DR
MADISON WI 53718

dated MAY 20, 2014, and served upon the company on SEPTEMBER 15, 2014, has been adopted as the final report, and has been placed on file as an official public record of this Office.

Dated at Madison, Wisconsin, this 8TH day of DECEMBER, 2014.

THEODORE K NICKEL
Commissioner of Insurance

STATE OF WISCONSIN
OFFICE OF THE COMMISSIONER OF INSURANCE

# MARKET CONDUCT EXAMINATION

OF

# 1ST AUTO & CASUALTY INSURANCE COMPANY

MAY 19-30, 2014

## TABLE OF CONTENTS


I. INTRODUCTION ..... 2

II. PURPOSE AND SCOPE ..... 5

III. PRIOR EXAMINATION RECOMMENDATIONS ..... 6

IV. CURRENT EXAMINATION FINDINGS ..... 10

- PRODUCER LICENSING ..... 10
- UNDERWRITING AND RATING ..... 11
- CLAIMS ..... 14
- POLICY FORMS AND RATES ..... 14

V. CONCLUSION ..... 15

VI. SUMMARY OF RECOMMENDATIONS ..... 16

VII. ACKNOWLEDGEMENT ..... 17

**State of Wisconsin** / OFFICE OF THE COMMISSIONER OF INSURANCE

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August 12, 2014

Honorable Theodore K. Nickel
Commissioner of Insurance
Madison, WI 53702

Commissioner:

Pursuant to your instructions and authorization, a compliance market conduct examination was conducted May 19 to May 30, 2014 of:

1ST AUTO & CASUALTY INSURANCE COMPANY
Madison, Wisconsin

and the following report of the examination is respectfully submitted.

## I. INTRODUCTION

The 1st Auto & Casualty Insurance Company (1st Auto or the company) is a Wisconsin domiciled property and casualty insurance company. The company was organized in 1991 as 1st Auto and commenced business September 25, 1991. The company is a wholly owned subsidiary of Wisconsin Reinsurance Corporation (WRC) and has intercompany services agreements with WRC. Services performed by WRC include accounting, data processing, marketing, receptionist, secretarial services, and any other services to be agreed upon by the parties. The company was initially capitalized with $3 million from the parent company. A stock offering by the parent corporation in 1997 added an additional $2 million to 1st Auto's surplus.

In both 2011 and 2012, the company reported written premium in Arkansas, Iowa, Illinois, Missouri, South Dakota, and Wisconsin. The following table summarizes the total direct national premium written in 2012 and 2011 as compared to the total direct premium written in Wisconsin.

**National Direct Premium Written to Wisconsin Direct Premium Written**

| Year | National Direct Premium Written | Wisconsin Direct Premium Written | WI As a Percentage of the National Premium |
|---|---|---|---|
| 2012 | $21,042,443 | $11,415,963 | 54.25% |
| 2011 | $20,010,744 | $11,640,129 | 58.17% |

The following tables summarize the premium earned and incurred losses in Wisconsin for 2012 and 2011 broken down by line of business.

**Wisconsin Direct Premium and Loss Summary**

| 2012 | | | | |
|---|---|---|---|---|
| **Line of Business** | **Premium Earned** | **% of WI Total** | **Losses Incurred** | **Pure Loss Ratio** |
| Private Passenger Auto | $9,508,890 | 83.29% | $7,423,504 | 78.07% |
| All Others | 975,641 | 10.26 | 100,000 | 10.25 |
| Total | $11,415,963 | | $7,964,538 | 69.77% |

| 2011 | | | | |
|---|---|---|---|---|
| **Line of Business** | **Premium Earned** | **% of WI Total** | **Losses Incurred** | **Pure Loss Ratio** |
| Private Passenger Auto | $9,797,116 | 84.17% | $5,319,132 | 54.29% |
| All Others | 986,364 | 8.47 | 1,200,000 | 121.66 |
| Total | $11,640,129 | | $6,728,420 | 57.80% |

Direct written premium for 2012 in Wisconsin was 58.17% of the national premium, and the direct written premium in Wisconsin for 2011 was 54.25% of the national premium. The majority of the premium earned by the company in 2011 and 2012 was private passenger auto.

In 2012, the company ranked as the 50th largest writer of private passenger auto in Wisconsin. In 2011, the company ranked as the 46th largest writer of private passenger auto in Wisconsin.

The Office of the Commissioner of Insurance (OCI) received seven complaints against the company between January 1, 2011 through December 31, 2012. A complaint is defined as "a written communication received by the commissioner's office that indicates dissatisfaction with an insurance company or agent." The following table categorizes the

complaints received against the company by type of policy and complaint reason. There may be more than one type of coverage and/or reason for each complaint.

**Complaints Received**

| 2012 Complaint Data | | | | |
|---|---|---|---|---|
| | | | Claims | |
| **Coverage Type** | **No.** | **% Total** | **No.** | **% Total** |
| Personal Auto | 3 | 75% | 3 | 75% |
| All Others | 1 | 25% | 1 | 25% |
| Total | 4 | 100% | 4 | 100% |

| 2011 Complaint Data | | | | |
|---|---|---|---|---|
| | | | Claims | |
| **Coverage Type** | **No.** | **% Total** | **No.** | **% Total** |
| Personal Auto | 3 | 100% | 3 | 100% |
| Total | 3 | 100% | 3 | 100% |

## II. PURPOSE AND SCOPE

A compliance examination was conducted to determine whether the company's practices and procedures comply with the Wisconsin insurance statutes and rules. The examination focused on the period from January 1, 2011 through December 31, 2012. In addition, the examination included a review of any subsequent events deemed important by the examiner-in-charge during the examination.

The examination included, but was not limited to, a review of recommendations from the previous 2009 examination, producer licensing, underwriting and rating, claims, company operations, and policy forms & rates.

The report is prepared on an exception basis and comments on those areas of the company's operations where adverse findings were noted.

## III. PRIOR EXAMINATION RECOMMENDATIONS

The previous market conduct examination of the company, as adopted January 22, 2012, contained 25 recommendations. Following are the recommendations and the examiners' findings regarding the company's compliance with each recommendation.

**Policy Forms and Rates**

1. It is recommended that the company implement a procedure to ensure that when filing forms via SERFF all polices where a readability score is required, as defined by s. Ins 6.07 (8)., Wis. Adm. Code, a minimum score meeting the requirements outlined in the rule is entered in the field designated for readability score.

Action: Compliance

2. It is recommended that the company correct the material typographical errors in the Miscellaneous Coverage section of the personal vehicle manual to ensure compliance with s. 628.34 (1) (a), Wis. Stat. and refile the corrected rules in accordance with s. 625.13, Wis. Stat.

Action: Compliance

3. It is recommended that the company submit rate and rule filings to the commissioner within 30 days after they become effective which contain all rates and supplementary rate information, in order to comply with s. 625.13 (1), Wis. Stat.

Action: Non-Compliance

4. It is recommended that the company file its complete rating algorithm in use at this time, with all of the possible rating factors for each coverage. For future filings, it is recommended that the company submit rate and rule filings to the commissioner within 30 days after they become effective which contain all rates and supplementary rate information, including the company's complete rating algorithm with all of the possible rating factors for each coverage, in order to comply with s. 625.13 (1), Wis. Stat.

Action: Non-Compliance

5. It is recommended that, prior to making forms available for use in Wisconsin, the company refile all previously approved forms including electronic forms, when changes to the form number, format, non-hypothetical data and/or other appropriate non-variable material on the form are made, to ensure compliance with s. 631.20, Wis. Stat., and s. Ins 6.05 (4) (a) 5., Wis. Adm. Code.

Action: Compliance

6. It is recommended that, prior to making forms available for use in Wisconsin, the company refile all previously approved forms when changes to the form number, format, non-hypothetical data and/or other appropriate non-variable material on the

form are made, to ensure compliance with s. 631.20, Wis. Stat., and s. Ins 6.05 (4) (a) 5., Wis. Adm. Code.

Action: Compliance

**Producer Licensing**

7. It is recommended that the company implement written procedures that include verification of recorded agent information in the company databases and verification that the data accurately reflect the status of the agent licensing and appointment information in order to ensure that only business is accepted from licensed and appointed agents as required by s. Ins 6.57(5)., Wis. Adm. Code.

Action: Non-Compliance

8. It is recommended that the company develop and implement written procedures to include verification that the recorded agent information in company databases accurately reflects the status of the agent licensing and appointment information as reported to OCI, in order to ensure that only business is accepted from licensed and appointed agents as required by s. Ins 6.57 (5)., Wis. Adm. Code.

Action: Compliance

9. It is recommended that the company implement a more thorough and accurate procedure to verify a formal written demand for the return of all indicia of agency at the time of the termination of the individuals appointment is provide to the agent representing the company and that said notice advise the individual that he or she may not act as the company's representative in order to comply with s. Ins 6.57 (2)., Wis. Adm. Code.

Action: Compliance

10. It is recommended that the company develop and implement a procedure to ensure that the correct reason for an agent termination is reported to the Commissioner in order to avoid an unfair marketing practice as defined by s. 628.34 (1), (a), Wis. Stat.

Action: Compliance

**Underwriting and Rating**

11. It is recommended that the company revise its underwriting guidelines, including the cheat sheet, to remove age requirements in order to ensure compliance with s. Ins 6.54 (3)., Wis. Adm. Code and to avoid unfair discrimination under s. 632.35, Wis. Stat.

Action: Non-Compliance

12. It is recommended that the company revise its underwriting guideline for unemployed persons and verification of regular income to reflect the company's actual intent, in order to ensure compliance with s. 632.35, Wis. Stat.

Action: Compliance

13. It is recommended that the company revise its underwriting guidelines and the cancellation section of its manual to clarify that the company will not deny, cancel, or non-renew an automobile policy based on the applicant's or insured's suspended or revoked license unless the suspension or revocation is directly related to a motor vehicle violation, in order to ensure compliance with s. Ins 6.54 (3) (a) 1., Wis. Adm. Code.

Action: Compliance

14. It is recommended that the company revise its "'moved out of state letter" to provide adequate instructions to the policyholder for applying for insurance through the Wisconsin Automobile Insurance Plan, in order to comply with s. 631.36 (7) (a) 2, Wis. Stat.

Action: Compliance.

15. It is recommended the company implement a system to eliminate the use of abbreviations on cancellation/nonrenewal notices when explaining the "reason" for an action. It is further recommended that reference to a motor vehicle report (MVR) shall state the actual driving violation a termination is based on to ensure compliance with s. 631.36 (6), Wis. Stat.

Action: Compliance

16. It is recommended that the company implement a written procedure to retain copies of any cancellation/non-renewal notice in the company's file for three years in order to comply with s. Ins 6.80 (4) (b)., Wis. Adm. Code.

Action: Compliance

17. It is recommended that when cancelling or non-renewing a policy under ss. 631.36 (2) (b) or (4), Wis. Stat., the company include in the notice adequate instructions to the policyholder, for applying for insurance through a risk-sharing plan under ch. 619, Wis. Stat., if a risk-sharing plan exists under ch. 619 for the kind of coverage being canceled or non-renewed, in order to ensure compliance with s. 631.36 (7), Wis. Stat. The information provided shall also include the correct address for the risk-sharing plan.

Action: Compliance

18. It is recommended that the company issue policies using only rates that have been filed with the commissioner within 30 days after they become effective, in order to comply with s. 625.13 (1), Wis. Stat.

Action: Compliance

19. It is recommended that the company file the company's Premier Plus, Optimal Plus and Shield tier rate factors in use at this time. For future filings, it is recommended that the company submit rate and rule filings to the commissioner within 30 days

after they become effective which contain all rates and supplementary rate information, including the company's Premier Plus, Optimal Plus and Shield tier rate factors, in order to comply with s. 625.13 (1), Wis. Stat.

Action: Compliance

**Company Operations and Management**

20. It is recommended that the company develop and conduct privacy policy training for all staff to ensure compliance with the requirements of ch. Ins 25, Wis. Adm. Code.

Action: Compliance

21. It is recommended that the company develop and conduct privacy policy training for all agents appointed with the company to ensure compliance with the requirements of ch. Ins 25, Wis. Adm. Code.

Action: Compliance

22. It is recommended that the company conduct an audit of the company privacy policy to ensure compliance with ch. Ins 25 of the Wis. Adm. Code, and that the company implement an audit schedule to ensure continued compliance with ch. Ins 25, Wis. Adm. Code.

Action: Compliance

23. It is recommended that the company develop a system to verify and enforce company privacy requirements as they apply to persons/organizations acting on the company's behalf to ensure compliance with the requirements of ch. Ins 25, Wis. Adm. Code.

Action: Compliance

24. It is recommended that the company include specific language in their WRC acknowledgement form addressing the company's privacy policy and outlining the consequences of non-compliance with that policy in order to ensure compliance with the requirements of ch. Ins 25, Wis. Adm. Code.

Action: Compliance

25. It is recommended that the company implement a system to review and verify the safeguards that listed agents have in place to keep personal information confidential in order to ensure compliance with the requirements of ch. Ins 25, Wis. Adm. Code.

Action: Compliance

## IV. CURRENT EXAMINATION FINDINGS

### Producer Licensing

The company uses independent agencies to market insurance products and agents must be affiliated with a mutual that the parent company, WRC, reinsures in order to represent 1st Auto. To review the company's obligation to notify the Commissioner of producers that are appointed or terminated, the examiners requested that the company provide a list consisting of all producers appointed to represent the company as of the end of the period of review. The company's list was then compared to the Commissioners database of producers appointed to represent the company as of that date. Internal producer licensing procedures of the company were also reviewed by examiners. In addition, the examiners reviewed 100 files where the agent was appointed to represent the company and/or the relationship with the company was terminated during the examination period of review. The following exceptions were noted:

The examiners compared the company's data with the OCI's data and found 13 producers who were not shown as appointed in the company's data that were shown as appointed in OCI records. Section 628.11, Wis. Stat., states in part that an insurer must notify OCI of all producer appointments and terminations. Section Ins 6.57 (2)., Wis. Adm. Code states in part that notice of termination of appointment of individual intermediary in accordance with s. 628.11, Wis. Stat. shall be filed prior to or within 30 calendar days of the termination date with the Office of the Commissioner of Insurance.

1. **Recommendation:** It is again recommended that the company implement written procedures to ensure that the agent information recorded in the company databases accurately reflect the status of the agent licensing and appointment information recorded in the OCI database in order to ensure that business is only accepted from properly licensed and appointed agents as required by s. Ins. 6.57 (5)., Wis. Adm. Code.

**Underwriting and Rating**

The examiners reviewed a random sample of 25 new business private passenger automobile policies to verify that the company is issuing policies using rates and rate-related rules that have been filed for use in Wisconsin.

The examiners found that the company requires specific credit scores to qualify for its rating tiers. In review of the files, 7 files were found with 2 named insureds and 2 available credit scores. The filed rules do not specifically indicate which credit score, the higher or lower, qualifies the policyholders for the specific tier. Section 625.13 (1), Wis. Stat. states that every authorized insurer and every rate service organization under s. 625.31, Wis. Stat. which has been designated by any insurer for the filing of rates under s. 625.15 (2), Wis. Stat. shall file with the commissioner all rates and supplementary rate information and all changes and amendments thereof made by it for use in this state within 30 days after they become effective.

In addtion, the examiners found one file where the company could not access the policyholder's credit score, yet the policyholder was placed in a specific rating tier. The filed rule advises that if a credit score cannot be accessed, the agent, etc. should call the underwriting department for rating. Upon interviewing the underwriting department, the examiner was informed that the company follows NAIC's model for rating when there is no credit score. The company rule is to assign the named insured the highest eligible tier available based on driving record eligibility. Pursuant to s. 625.13 (1), Wis. Stat. every authorized insurer and every rate service organization licensed under s. 625.31, Wis. Stat. which has been designated by any insurer for the filing of rates under s. 625.15 (2), Wis. Stat. shall file with the commissioner all rates and supplementary rate information and all changes and amendments thereof made by it for use in this state within 30 days after the become effective. Section 625.02 (3), Wis. Stat. defines supplementary rate information as any manual or plan of rates, statistical plan,

classification, rating schedule, minimum premium, policy fee, rating rule, rate-related underwriting rule and any other information prescribed by rule of the commissioner.

2. **Recommendation:** It is recommended that the company file a rule regarding rating using the highest credit score when there are two named insureds in order to comply with s. 625.13 (1), Wis. Stat. In addition, it is recommended that the company file its supplementary rate information, to include the rule for rating tier assignment when there is no credit score available in order to comply with s. 625.02 (3), Wis. Stat.

The examiners found in one of the files a case where the policyholder was rated in the optimal plus rating tier, which requires a credit score of 630. The policyholder's credit score at the time the policy became effective was 623. Section 628.34 (3) (a), Wis. Stat. states that no insurer may unfairly discriminate among policyholders by charging different premiums or by offering different terms of coverage except on the basis of classifications related to the nature of the risk covered or the expenses involved.

3. **Recommendation:** It is recommended that the company's underwriters quality check agents' premium quotes, and follow its written credit score underwriting rules in order to comply with s. 628.34 (3) (a), Wis. Stat.

The examiners found 13 files with effective dates on or after November, 1, 2011, where the filed rates omitted 2010 vehicle rating factors for comprehensive and collision coverages. The company did not submit an additional filing to include the comprehensive and collision rates for 2010 vehicles. Pursuant to s. 625.13 (1), Wis. Stat., every authorized insurer and every rate service organization licensed under s. 625.31, Wis. Stat. which had been designated by any insurer for filing of rates under s. 625.15 (2), Wis. Stat. shall file with the commissioner all rates and supplementary rate information and all changes and amendments thereof made by it for use in this state within 30 days after they become effective.

4. **Recommendation:** It is again recommended that the company follow its written rate filing procedures to ensure that it files with the commissioner all rates and supplementary rate information in order to comply with s. 625.13 (1), Wis. Stat.

The examiners reviewed the underwriting manual for the definition of business use of private passenger vehicles. Business use is defined based on the occupation. More specifically, if the personal vehicle is being used for newspaper or postal mail delivery. (for mail delivery, the insured must be employed by the Post Office) and the vehicle has liability only, the vehicle is not rated for business use. If the vehicle has physical damage coverage, then the vehicle is rated for business use. In contrast, if the personal vehicle is being used for pizza delivery, the vehicle would be rated business use regardless of whether the personal vehicle has placement of liability or physical damage coverage. The examiners were informed that the federal government covers liability when a Postal Service employee is using his or her vehicle for work. Therefore, the underwriting rationale is that business use is then covered and that is why it is not rated as business use. However, this does not apply to newspaper delivery which is treated the same as postal mail delivery. Section 628.34 (3), Wis. Stat. states that no insurer may unfairly discriminate among policyholders by charging different premiums or by offering different terms of coverage except on the basis of classifications relate to the nature and the degree of the risk covered or the expenses involved.

5. **Recommendation:** It is recommended that the company revise the language of the underwriting rule to remove newspaper delivery from the exception regarding Postal Service employees to clearly state that the exception only applies to federal government employees who are covered when driving a vehicle for work purposes in order to comply with s. 628.34 (3), Wis. Stat.

The examiners reviewed a random sample of 100 new business files, which included a review of 100 new business applications. It was found that it is the company's practice to allow their agents to retain copies of the signed applications. The examiners found the company was unable to produce a copy of 4 applications. Section Ins. 6.61(8) (d)., Wis. Adm. Code states in part that each intermediary shall maintain policyholder records for a three-year period.

6. **Recommendation:** It is recommended that the company develop and implement a business practice to inform its intermediaries in writing of the requirements of s. Ins 6.61 (8) (d), Wis. Adm. Code., that each intermediary

shall maintain, for a three-year period, policyholder records, including original applications

**Claims**

The examiners reviewed 142 private passenger automobile claims. Of these claims, 100 were paid private passenger automobile claims and 42 were private passenger automobile claims not paid. The company's claim handling practices and procedures were also reviewed. All claims were processed in a timely manner and no claims paid problems were noted. No exceptions were noted within the files reviewed.

**Policy Forms and Rates**

The company is using independently filed forms along with ISO forms, AAIS forms and ACORD applications. The examiners reviewed personal lines policy forms submitted by the company and used during the period of review in order to verify that the provisions of the policy forms comply with Wisconsin insurance laws and regulations. No exceptions were noted.

## V. CONCLUSION

There were four previous recommendations from the 2009 examination that were found to be in non-compliance relating to policy forms and rates filing, producer licensing, and underwriting and rating.

There were two recommendations that resulted in non-compliance due to the company not submitting all rate and rule filings to OCI as required. One recommendation resulted in non-compliance as a result of the company not verifying agent appointment and licensing information. The other previous recommendation that resulted in non-compliance was due to age requirements not being corrected on the company's underwriting cheat sheets resulting in possible discrimination.

A total of six recommendations were made as a result of this compliance examination relating to the company's need to write and/or modify producer licensing procedures and underwriting and rating procedures.

There was one recommendation in relation to producer licensing. The company must implement written procedures to ensure that the agent information recorded in the company databases accurately reflect the status of the agent licensing and appointment information recorded in the OCI database.

There were five recommendations in relation to underwriting and rating. The company needs to revise its rules to be consistent with all applicants. Rates and rules used must be filed in compliance with s. 631.13 (1), Wis. Stat. Records must be maintained in accordance with s. ins. 6.61, Wis. Adm. Code.

## VI. SUMMARY OF RECOMMENDATIONS

### Producer Licensing

Page 10 1. It is again recommended that the company implement written procedures to ensure that the agent information recorded in the company databases accurately reflect the status of the agent licensing and appointment information recorded in the OCI database in order to ensure that business is only accepted from properly licensed and appointed agents as required by s. Ins. 6.57 (5)., Wis. Adm. Code.

### Underwriting and Rating

Page 12 2. It is recommended that the company file the rule regarding rating using the highest credit score when there are two named insureds in order to comply with s. 625.13 (1), Wis. Stat. In addition, it is further recommended that the company follow its underwriting rules regarding rating to avoid unfair discrimination in order to comply with s. 628.34 (3) (a), Wis. Stat.

Page 12 3. It is recommended that the company's underwriters quality check agents' premium quotes, and follow its written credit score underwriting rules in order to comply with s. 628.34 (3) (a), Wis. Stat.

Page 12 4. It is again recommended that the company follow its written rate filing procedures to ensure that it files with the commissioner all rates and supplementary rate information in order to comply with s. 625.13 (1), Wis. Stat.

Page 13 5. It is recommended that the company revise the language of the underwriting rule to remove newspaper delivery from the exception regarding Postal Service employees to clearly state that the exception only applies to federal government employees who are covered when driving a vehicle for work purposes in order to comply with s. 628.34 (3), Wis. Stat.

Page 13 6. It is recommended that the company develop and implement a business practice to inform its intermediaries in writing of the requirements of s. Ins 6.61 (8) (d)., Wis. Adm. Code., that each intermediary shall maintain, for a three-year period, policyholder records, including original applications.

## VII. ACKNOWLEDGEMENT

The courtesy and cooperation extended to the examiners during the course of the examination by the officers and employees of the company is acknowledged.

In addition, to the undersigned, the following representatives of the Office of the Commissioner of Insurance, state of Wisconsin, participated in the examination.

| Name | Title |
|---|---|
| Ellen Vigil MCM | Insurance Examiner |
| Rebecca Rebholz MCM | Insurance Examiner |
| Jaclyn de Medicci | Insurance Examiner |
| Katherine Otis MCM | Insurance Examiner |

Respectfully submitted,

Jennifer Harris MCM
Examiner-in-Charge